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Auditor's responsibility to detect and report errors and irregularities; Statement on auditing standards, 053

American Institute of Certified Public Accountants. Auditing Standards Board

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The Auditor's Responsibility to Detect and Report Errors and Irregularities

(Supersedes Statement on Auditing Standards No. 16, AICPA, Professional Standards, vol. 1, AU sec. 327.)

1. This Statement provides guidance on the independent auditor's responsibility for the detection of errors and irregularities in an audit of financial statements in accordance with generally accepted auditing standards. It describes factors that influence the auditor's ability to detect errors and irregularities and explains how the exercise of due care should give appropriate consideration to the possibility of errors or irregularities. It also provides guidance on the auditor's responsibility to communicate detected matters both within and outside the entity whose financial statements are under audit.

Definition of Errors and Irregularities

2. The term *errors* refers to *unintentional* misstatements or omissions of amounts or disclosures in financial statements. Errors may involve —

- Mistakes in gathering or processing accounting data from which financial statements are prepared.

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- Incorrect accounting estimates arising from oversight or misinterpretation of facts.
- Mistakes in the application of accounting principles relating to amount, classification, manner of presentation, or disclosure.¹

3. The term *irregularities* refers to *intentional* misstatements or omissions of amounts or disclosures in financial statements. Irregularities include fraudulent financial reporting undertaken to render financial statements misleading, sometimes called *management fraud*, and misappropriation of assets, sometimes called *defalcations*. Irregularities may involve acts such as the following:

- Manipulation, falsification, or alteration of accounting records or supporting documents from which financial statements are prepared
- Misrepresentation or intentional omission of events, transactions, or other significant information
- Intentional misapplication of accounting principles relating to amounts, classification, manner of presentation, or disclosure

4. The primary factor that distinguishes errors from irregularities is whether the underlying cause of a misstatement in financial statements is intentional or unintentional. Intent, however, is often difficult to determine, particularly in matters involving accounting estimates or the application of accounting principles. For example, an unreasonable accounting estimate may result from unintentional bias or may be an intentional attempt to misstate the financial statements.

The Auditor's Responsibility to Detect Errors and Irregularities

5. The auditor should assess the risk that errors and irregularities may cause the financial statements to contain a material misstatement.

¹Errors do not include the effect of accounting processes employed for convenience, such as maintaining accounting records on the cash basis or the tax basis and periodically adjusting those records to prepare financial statements in conformity with generally accepted accounting principles.

Based on that assessment, the auditor should design the audit to provide reasonable assurance of detecting errors and irregularities that are material to the financial statements.^{2,3}

6. The auditor's assessment of the risk of material misstatement of the financial statements requires the auditor to understand the characteristics of errors and irregularities that are discussed in the Appendix and the complex interaction of those characteristics. Based on that understanding, the auditor designs and performs appropriate audit procedures and evaluates the results.

7. Because of the characteristics of irregularities, particularly those involving forgery and collusion, a properly designed and executed audit may not detect a material irregularity. For example, generally accepted auditing standards do not require that an auditor authenticate documents, nor is the auditor trained to do so. Also, audit procedures that are effective for detecting a misstatement that is unintentional may be ineffective for a misstatement that is intentional and is concealed through collusion between client personnel and third parties or among management or employees of the client.

8. The auditor should exercise (a) due care in planning, performing, and evaluating the results of audit procedures, and (b) the proper degree of professional skepticism to achieve reasonable assurance that material errors or irregularities will be detected. Since the auditor's opinion on the financial statements is based on the concept of reasonable assurance, the auditor is not an insurer and his report does not constitute a guarantee. Therefore, the subsequent discovery that a material misstatement exists in the financial statements does not, in and of itself, evidence inadequate planning, performance, or judgment on the part of the auditor.

²The concept of reasonable assurance is recognized in the third standard of fieldwork, "Sufficient competent evidential matter is to be obtained through inspection, observation, inquiries and confirmation to afford a reasonable basis for an opinion regarding the financial statements under examination" and is discussed in Statement on Auditing Standards No. 31, *Evidential Matter* (AICPA, *Professional Standards*, vol. 1, AU sec. 326) and SAS No. 39, *Audit Sampling* (AICPA, *Professional Standards*, vol. 1, AU sec. 350).

³The auditor's responsibility for detecting misstatements resulting from illegal acts, as defined in SAS No. 54, *Illegal Acts by Clients*, having a direct and material effect on the determination of financial statement amounts is the same as that for other errors and irregularities.

Consideration of the Possibility of Material Misstatements in Audit Planning

9. In developing an audit plan, the auditor should consider factors influencing audit risk that relates to several or all account balances and obtain an understanding of the internal control structure.⁴ These matters often have effects pervasive to the financial statements taken as a whole and also influence the auditor's consideration of risk at the account balance or class-of-transactions level.

Consideration of Audit Risk at the Financial Statement Level

10. An assessment of the risk of material misstatements should be made during planning. The auditor's understanding of the internal control structure should either heighten or mitigate the auditor's concern about the risk of material misstatements. The factors considered in assessing risk should be considered in combination to make an overall judgment; the presence of some factors in isolation would not necessarily indicate increased risk. Factors such as those listed below may be considered.

Management Characteristics

- Management operating and financing decisions are dominated by a single person.
- Management's attitude toward financial reporting is unduly aggressive.
- Management (particularly senior accounting personnel) turnover is high.
- Management places undue emphasis on meeting earnings projections.
- Management's reputation in the business community is poor.

Operating and Industry Characteristics

- Profitability of entity relative to its industry is inadequate or inconsistent.
- Sensitivity of operating results to economic factors (inflation, interest rates, unemployment, etc.) is high.

⁴See SAS No. 55, *Consideration of the Internal Control Structure in a Financial Statement Audit*.

- Rate of change in entity's industry is rapid.
- Direction of change in entity's industry is declining with many business failures.
- Organization is decentralized without adequate monitoring.
- Internal or external matters that raise substantial doubt about the entity's ability to continue as a going concern are present. (See SAS No. 59, *The Auditor's Consideration of an Entity's Ability to Continue as a Going Concern*.)

Engagement Characteristics

- Many contentious or difficult accounting issues are present.
- Significant difficult-to-audit transactions or balances are present.
- Significant and unusual related party transactions not in the ordinary course of business are present.
- Nature, cause (if known), or the amount of known and likely misstatements detected in the audit of prior period's financial statements is significant.
- It is a new client with no prior audit history or sufficient information is not available from the predecessor auditor.

11. The size, complexity, and ownership characteristics of the entity have a significant influence on the risk factors considered to be important. For example, for a large entity, the auditor would ordinarily give consideration to factors that constrain improper conduct by senior management, such as the effectiveness of the board of directors, the audit committee or others with equivalent authority and responsibility⁵, and the internal audit function. Consideration would also be given to the measures taken to enforce a formal code of conduct and the effectiveness of the budgeting or responsibility reporting system. For a small entity some of these matters might be considered inapplicable or unimportant, particularly if the auditor's past experience with the entity has been that effective owner-manager or trustee involvement creates a good control environment.

⁵For entities that do not have audit committees, the phrase "others with equivalent authority and responsibility" may include the board of directors, the board of trustees, or the owner in owner-managed entities.

12. The auditor should assess the risk of management misrepresentation by reviewing information obtained about risk factors and the internal control structure. Matters such as the following may be considered:

- Are there known circumstances that may indicate a management predisposition to distort financial statements, such as frequent disputes about aggressive application of accounting principles that increase earnings, evasive responses to audit inquiries, or excessive emphasis on meeting quantified targets that must be achieved to receive a substantial portion of management compensation?
- Are there indications that management has failed to establish policies and procedures that provide reasonable assurance of reliable accounting estimates, such as personnel who develop estimates appearing to lack necessary knowledge and experience, supervisors of these personnel appearing careless or inexperienced, or there is a history of unreliable or unreasonable estimates?
- Are there conditions that indicate lack of control of activities, such as constant crisis conditions in operating or accounting areas, disorganized work areas, frequent or excessive back orders, shortages, delays, or lack of documentation for major transactions?
- Are there indications of a lack of control over computer processing, such as a lack of controls over access to applications that initiate or control the movement of assets (for example, a demand deposit application in a bank), high levels of processing errors, or unusual delays in providing processing results and reports?
- Are there indications that management has not developed or communicated adequate policies and procedures for security of data or assets, such as not investigating employees in key positions before hiring, or allowing unauthorized personnel to have ready access to data or assets?

13. The auditor should consider the effect of the matters described in paragraphs 10 to 12 on the overall audit strategy and the expected conduct and scope of the audit.

The Auditor's Response to Risk at the Financial Statement Level

14. The auditor's overall judgment about the level of risk in an engagement may affect engagement staffing, extent of supervision,

overall strategy for expected conduct and scope of audit, and degree of professional skepticism applied. Thus, the auditor's assessment of risk may affect audit planning in one or more of the following ways. The experience and training of personnel assigned significant engagement responsibilities should be commensurate with the auditor's assessment of the level of risk for the engagement. Ordinarily, higher risk requires more experienced personnel or more extensive supervision by the auditor with final responsibility for the engagement during both the planning and the conduct of the engagement. Higher risk may cause the auditor to expand the extent of procedures applied, apply procedures closer to or as of the balance sheet date, particularly in critical audit areas, or modify the nature of procedures to obtain more persuasive evidence. Higher risk will also ordinarily cause the auditor to exercise a heightened degree of professional skepticism in conducting the audit (see paragraphs 16 to 21).

The Auditor's Consideration of Audit Risk at the Balance or Class Level

15. The following matters are examples of factors that may influence the auditor's consideration of risk of material misstatement related to particular assertions at the balance or class level:⁶

- Effect of risk factors identified at the financial statement or engagement level on the particular account balance or transaction class
- Complexity and contentiousness of accounting issues affecting balance or class
- Frequency or significance of difficult-to-audit transactions affecting balance or class
- Nature, cause, and amount of known and likely misstatements detected in the balance or class in the prior audit
- Susceptibility of related assets to misappropriation
- Competence and experience of personnel assigned to processing data that affect the balance or class

⁶Additional factors relating to risk assessment are found in SAS No. 47, *Audit Risk and Materiality in Conducting an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec. 312).

- Extent of judgment involved in determining the total balance or class
- Size and volume of individual items constituting the balance or class
- Complexity of calculations affecting the balance or class

Professional Skepticism

16. An audit of financial statements in accordance with generally accepted auditing standards should be planned and performed with an attitude of professional skepticism. The auditor neither assumes that management is dishonest nor assumes unquestioned honesty. Rather, the auditor recognizes that conditions observed and evidential matter obtained, including information from prior audits, need to be objectively evaluated to determine whether the financial statements are free of material misstatement.

17. Management integrity is important because management can direct subordinates to record transactions or conceal information in a manner that can materially misstate financial statements. When approaching difficult-to-substantiate assertions, the auditor should recognize the increased importance of his consideration of factors that bear on management integrity. A presumption of management dishonesty, however, would be contrary to the accumulated experience of auditors. Moreover, if dishonesty were presumed, the auditor would potentially need to question the genuineness of all records and documents obtained from the client and would require conclusive rather than persuasive evidence to corroborate all management representations. An audit conducted on these terms would be unreasonably costly and impractical.

Professional Skepticism in Audit Planning

18. Whenever the auditor has reached a conclusion that there is significant risk of material misstatement of the financial statements, the auditor reacts in one or more ways. The auditor should consider this assessment in determining the nature, timing, or extent of procedures, assigning staff, or requiring appropriate levels of supervision. The auditor may identify specific transactions involving senior man-

agement and confirm the details with appropriate external parties and review in detail all material accounting entries prepared or approved by senior management.

19. The auditor should consider whether accounting policies are acceptable in the circumstances. However, when the auditor has reached a conclusion that there is significant risk of intentional distortion of financial statements, the auditor should recognize that management's selection and application of significant accounting policies, particularly those related to revenue recognition, asset valuation, and capitalization versus expensing, may be misused. Increased risk of intentional distortion of the financial statements should cause greater concern about whether accounting principles that are otherwise generally accepted are being used in inappropriate circumstances to create a distortion of earnings. For example, management might use the percentage of completion method in circumstances that do not justify its use to misstate operating results.

20. When evaluation at the financial statement level indicates significant risk, the auditor requires more or different evidence to support material transactions than would be the case in the absence of such risk. For example, the auditor may perform additional procedures to determine that sales are properly recorded, giving consideration to the possibility that the buyer has a right to return the product. Transactions that are both large and unusual, particularly at year-end, should be selected for testing.

Professional Skepticism in Performance of the Audit

21. In performing procedures and gathering evidential matter, the auditor continually maintains an attitude of professional skepticism. The performance of auditing procedures during the audit may result in the detection of conditions or circumstances that should cause the auditor to consider whether material misstatements exist. If a condition or circumstance differs adversely from the auditor's expectation, the auditor needs to consider the reason for such a difference. Examples of such conditions or circumstances are as follows:

- Analytical procedures disclose significant differences from expectations.
- Significant unreconciled differences between reconciliations of a control account and subsidiary records or between a physical count

and a related account are not appropriately investigated and corrected on a timely basis.

- Confirmation requests disclose significant differences or yield fewer responses than expected.
- Transactions selected for testing are not supported by proper documentation or are not appropriately authorized.
- Supporting records or files that should be readily available are not promptly produced when requested.
- Audit tests detect errors that apparently were known to client personnel, but were not voluntarily disclosed to the auditor.

When such conditions or circumstances exist, the planned scope of audit procedures should be reconsidered. As the number of differences from expectations or the frequency with which the auditor is unable to obtain satisfactory explanations increases, the auditor should consider whether the assessment of the risk of material misstatement of the financial statements made in the planning stage of the engagement is still appropriate.

Evaluation of Audit Test Results

22. The auditor should evaluate the significance of differences between the accounting records and the underlying facts and circumstances detected by the application of auditing procedures. The auditor should consider both the quantitative and qualitative aspects of these matters and whether they are indicative of an error or an irregularity. Often a particular matter considered in isolation cannot be identified as an error or irregularity; nevertheless, this evaluation is important. Because irregularities are intentional, they have implications beyond their direct monetary effect and the auditor needs to consider the implications for other aspects of the audit.

23. The auditor's objective is to reach a conclusion on whether the financial statements, taken as a whole, are materially misstated. The auditor should accumulate potential audit adjustments during the audit and summarize and evaluate the combined effect. In this regard, the auditor may designate an amount below which potential audit adjustments need not be accumulated. This amount would be set so that any such adjustments, either individually or when aggregated

with other adjustments, would not be material to the financial statements.

24. If the auditor has determined that an audit adjustment is, or may be, an irregularity, but has also determined that the effect on the financial statements could not be material, the auditor should —

- a.* Refer the matter to an appropriate level of management that is at least one level above those involved.
- b.* Be satisfied that, in view of the organizational position of the likely perpetrator, the irregularity has no implications for other aspects of the audit or that those implications have been adequately considered.

For example, irregularities involving misappropriation of cash from a small imprest fund would normally be of little significance because both the manner of operating the fund and its size would tend to establish a limit on the amount of loss and the custodianship of such a fund is normally entrusted to a relatively low-level employee.

25. If the auditor has determined that an audit adjustment is, or may be, an irregularity and has either determined that the effect could be material or has been unable to evaluate potential materiality, the auditor should —

- a.* Consider the implications for other aspects of the audit.
- b.* Discuss the matter and the approach to further investigation with an appropriate level of management that is at least one level above those involved.
- c.* Attempt to obtain sufficient competent evidential matter to determine whether, in fact, material irregularities exist and, if so, their effect.
- d.* If appropriate, suggest that the client consult with legal counsel on matters concerning questions of law.

The Effect of Irregularities on the Audit Report

26. If the auditor has concluded that the financial statements are materially affected by an irregularity, the auditor should insist that the financial statements be revised and, if they are not, express a qualified

or an adverse opinion on the financial statements, disclosing all substantive reasons for his opinion.

27. If the auditor is precluded from applying necessary procedures, or if, after the application of extended procedures, the auditor is unable to conclude whether possible irregularities may materially affect the financial statements, the auditor should —

- a. Disclaim or qualify an opinion on the financial statements.
- b. Communicate his findings to the audit committee or the board of directors.

If the client refuses to accept the auditor's report as modified for the circumstances described above, the auditor should withdraw from the engagement and communicate the reasons for withdrawal to the audit committee or board of directors. Whether the auditor concludes that withdrawal from the engagement is appropriate in other circumstances depends on the diligence and cooperation of senior management and the board of directors in investigating the circumstances and taking appropriate remedial action. For example, if the auditor is precluded by the client from obtaining reasonably available evidential matter, withdrawal ordinarily would be appropriate. However, because of the variety of circumstances that may arise, it is not possible to describe all those circumstances when withdrawal would be appropriate.

Communications Concerning Errors or Irregularities

28. For the audit committee⁷ to make the informed judgments necessary to fulfill its responsibility for the oversight of financial reporting, the auditor should assure himself that the audit committee is adequately informed about any irregularities of which the auditor becomes aware during the audit unless those irregularities are clearly inconsequential.⁸ For example, a minor defalcation by an employee at a low level in the organization might be considered inconsequential.

⁷ See note 5.

⁸ The auditor's responsibility to communicate errors within certain entities whose financial statements are under audit is described in SAS No. 61, *Communication With Audit Committees*.

However, irregularities involving senior management of which the auditor becomes aware should be reported directly to the audit committee. Irregularities that are individually immaterial may be reported to the audit committee on an aggregate basis, and the auditor may reach an understanding with the audit committee on the nature and amount of reportable irregularities.

29. Disclosure of irregularities to parties other than the client's senior management and its audit committee or board of directors is not ordinarily part of the auditor's responsibility, and would be precluded by the auditor's ethical or legal obligation of confidentiality unless the matter affects his opinion on the financial statements. The auditor should recognize, however, that in the following circumstances a duty to disclose outside the client may exist:

- a. When the entity reports an auditor change under the appropriate securities law on Form 8-K⁹
- b. To a successor auditor when the successor makes inquiries in accordance with SAS No. 7, *Communications Between Predecessor and Successor Auditors* (AICPA, *Professional Standards*, vol. 1, AU sec. 315)¹⁰
- c. In response to a subpoena
- d. To a funding agency or other specified agency in accordance with requirements for the audits of entities that receive financial assistance from a government agency

Because potential conflicts with the auditor's ethical and legal obligations for confidentiality may be complex, the auditor may wish to consult with legal counsel before discussing irregularities with parties outside the client.

Responsibilities in Other Circumstances

30. This Statement describes the auditor's responsibilities to detect and report errors and irregularities in an audit of a complete set of

⁹ Disclosure to the Securities and Exchange Commission may be necessary if, among other matters, the auditor withdraws because the board of directors has not taken appropriate remedial action. Such failure may be a reportable disagreement on Form 8-K.

¹⁰ In accordance with SAS No. 7, communications between predecessor and successor auditors require the specific permission of the client.

financial statements made in accordance with generally accepted auditing standards. In other engagements, the auditor's responsibilities may be more extensive or more restricted, depending on the terms of the engagement.

31. The auditor may accept an engagement that necessitates a more extensive responsibility to detect or report irregularities. For example, in an audit in accordance with *Standards for Audit of Governmental Organizations, Programs, Activities, and Functions, 1981 Revision*, issued by the U.S. General Accounting Office, the auditor should be aware that such standards go beyond generally accepted auditing standards as they relate to notification when the audit indicates that irregularities may exist. These standards require the auditor not only to promptly report instances of irregularities to the audited entity's management, but also to report the matter to the funding agency or other specified agency.

32. When an examination does not encompass a complete set of financial statements or a complete individual financial statement, or when the scope is less extensive than an audit in accordance with generally accepted auditing standards, the auditor's ability to detect material misstatements may be considerably reduced. For example, in an engagement to report on specified elements, accounts, or items of financial statements, the auditor's procedures focus on the specific element, account, or item and the special purpose of the engagement. In these circumstances, the auditor's assessment of risk at the financial statement level and other aspects of the examination that relate to the entity and its financial statements taken as a whole is necessarily more restricted.

Effective Date

33. This Statement is effective for audits of financial statements for periods beginning on or after January 1, 1989. Early application of the provisions of this Statement is permissible.

Appendix

Characteristics of Errors and Irregularities

1. Characteristics of errors and irregularities that are relevant because of their potential influence on the auditor's ability to detect such matters are materiality of the effect on financial statements, level of management or employees involved, extent and skillfulness of any concealment, relationship to established specific control procedures, and the specific financial statements affected.

Materiality

2. SAS No. 47, *Audit Risk and Materiality in Conducting an Audit* (AICPA, *Professional Standards*, vol. 1, AU sec 312.04), states that "financial statements are materially misstated when they contain errors or irregularities whose effect, individually or in the aggregate, is important enough to cause them not be presented fairly in conformity with generally accepted accounting principles." SAS No. 47, paragraph 13, also states: "The auditor generally plans the audit primarily to detect errors that he believes could be large enough, individually or in the aggregate, to be quantitatively material to the financial statements." As used in SAS No. 47, the term *errors* refers to both errors and irregularities.

3. In planning the audit, the auditor is concerned with matters that could be material to the financial statements. An audit in accordance with generally accepted auditing standards may detect errors or irregularities that are not material to the financial statements, but such an audit can provide no assurance of detecting immaterial errors or irregularities. In this regard, there is no important distinction between errors and irregularities. There is a distinction, however, in the auditor's response to detected matters. Generally, an isolated, immaterial error in processing accounting data or applying accounting principles is not significant to the audit. In contrast, detection of an irregularity requires consideration of the implications for the integrity of management or employees and the possible effect on other aspects of the audit.

Level of Involvement

4. An irregularity may be caused by an employee or by management and, if by management, by a relatively high or low level of management. The experience of auditors indicates that the level of involvement often combines with

other characteristics in ways that have an influence on the auditor's ability to detect.

5. Defalcations by employees are often immaterial in amount and concealed in a manner that does not misstate net assets or net income. This type of irregularity can be more efficiently and effectively dealt with by an effective internal control structure and fidelity bonding of employees.

6. Material irregularities perpetrated by senior levels of management, including an owner-manager of a small business, are infrequent, but when they do occur they often engender widespread attention. These irregularities may not be susceptible to prevention or detection by specific control procedures because senior management is above the controls that deter employees or may override these controls with relative ease. Culture, custom, and the corporate governance system inhibit irregularities by senior management, but are not infallible deterrents. For this reason, an audit in accordance with generally accepted auditing standards necessarily gives due consideration to factors that bear on management integrity and the control environment.

Concealment

7. Concealment is any attempt by the perpetrator of an irregularity to reduce the likelihood of detection. Concealment usually involves manipulation of accounting records or supporting documents to disguise the fact that the accounting records are not in agreement with the underlying facts and circumstances. Concealment can be skillful and elaborate or clumsy and limited. The auditor's ability to detect a concealed irregularity depends on the skillfulness of the perpetrator, the frequency and extent of manipulation, and the relative size of individual amounts manipulated.

8. Forgery may be used to create false signatures, other signs of authenticity, or entire documents. Collusion may result in falsified confirmations or other evidence of validity. Also, unrecorded transactions are normally more difficult to detect than concealment achieved by manipulation of recorded transactions. However, the effect of concealment on the ability to detect an irregularity is dependent on the particular circumstances. For example, an attempt to mislead users of financial statements by recording large, fictitious revenue transactions late in the period without supporting documentation would be more readily detected than fictitious revenue transactions spread throughout the period, individually immaterial in amount, and supported by legitimate-appearing invoices and shipping documents. Moreover, both of these irregularities might be extremely difficult, if not impossible, to detect if collusion of customers is added to the concealment scheme.

Internal Control Structure

9. A lack of control procedures could permit an error or irregularity to occur repeatedly and the repeated occurrence could accumulate to a material amount. However, the auditor may not detect an error or irregularity that results from a nonrecurring breakdown of a specific control procedure because a rare item permitted by temporary conditions may not come to light in the performance of analytical or other procedures.

10. Irregularities may also be perpetrated or concealed by circumvention of specific control procedures or may be perpetrated by a level of management above specific control procedures. These types of irregularities are generally more difficult for an auditor to detect. However, the auditor should consider whether there are circumstances or factors that indicate a higher risk of these types of irregularities and modify auditing procedures accordingly.

Financial Statement Effect

11. Other matters remaining equal, errors or irregularities that involve overstatement will generally be more readily detected than those that involve understatement because the audit evidence available is more reliable for detecting such errors or irregularities. Also, misstatements that are charged to the income statement are less likely to be detected than those that are concealed in the balance sheet, because the process of comparing recorded accountability with the existing assets should detect significant errors concealed in the balance sheet.

Summary

12. The foregoing discussion considers characteristics of errors and irregularities individually and explains the effect an individual characteristic tends to have on the auditor's detection ability. However, these characteristics may interact in particular circumstances in ways that also affect the auditor's ability to detect a specific error or irregularity.

The Statement entitled The Auditor's Responsibility to Detect and Report Errors and Irregularities was adopted by the assenting votes of twenty members of the board, of whom one, Mr. Clancy, assented with qualification. Mr. Gunther dissented.

Mr. Clancy qualifies his assent to the issuance of this Statement because, although he endorses the extension of the auditor's responsibilities to detect and report material misstatements of the financial statements, he believes that the inclusion of the reasonable assurance concept in the auditor's responsibility statement diminishes an otherwise affirmative acknowledgement that the audit should be designed to detect material misstatements of the financial statements.

Mr. Gunther dissents because he has not seen evidence that SAS No. 16, *The Independent Auditor's Responsibility for the Detection of Errors or Irregularities*, is inadequate.

Auditing Standards Board (1986–1987)

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